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87-962

No. ——

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

SOUTHERN UNION COMPANY,
Petitioner,

v.

CONSOLIDATED OIL & GAS, INC.,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW MEXICO

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QUESTIONS PRESENTED

(1) Whether an award of damages for negligent misrepresentation in connection with the sale of interstate gas represents an unlawful increase in the price of gas under *Arkansas Louisiana Gas Co.* v. *Hall*, where those damages are measured by the precise difference between federal ceiling prices for natural gas and higher intrastate prices.

(2) Whether the filed rate doctrine applies to statutorily-set price ceilings for natural gas sales.

(3) Whether a state standard of negligence which assumes that a federally regulated producer may be justifiably ignorant of the jurisdictional status of its gas undermines and conflicts with paramount federal regulation of interstate natural gas sales.

(4) Whether the tort of negligent misrepresentation falls within the category of "affirmative misconduct" identified by this Court as a possible exception to the preemption holding in *Arkansas Louisiana Gas Co.* v. *Hall.*

PARTIES TO THE PROCEEDINGS

The parties to these proceedings are petitioner Southern Union Company and respondent Consolidated Oil & Gas, Inc.[1]

STATEMENT REQUIRED BY RULE 28.1

The following listed entities are subsidiaries of Southern Union's wholly-owned subsidiaries:

(1) First Bankers Trust and Savings Association of Midland, Texas (a Texas chartered savings and loan association) is a wholly-owned subsidiary of Southern Union Financial Corporation.

(2) Unifirst of Texas, Inc. (a Texas corporation) is a wholly-owned subsidiary of First Bankers Trust and Savings Association of Midland, Texas.

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[1] A former Southern Union subsidiary, Southern Union Gathering Company, and a former Southern Union division, Gas Company of New Mexico, were parties to the underlying state court litigation. However, in 1985, Southern Union sold its New Mexico utility properties operated by its Gas Company of New Mexico division to Public Service Company of New Mexico ("PNM"). As part of the same transaction, Southern Union also sold all of the stock of Gathering Company to a wholly-owned subsidiary of PNM. Under the terms of the sale, Southern Union assumed liability for and agreed to indemnify PNM for the payment of damages awarded below. Gathering Company and Gas Company of New Mexico are no longer real parties in interest to this litigation.

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PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW MEXICO

Southern Union Company respectfully petitions that a writ of certiorari be issued to review an opinion and order of the Supreme Court of the State of New Mexico.

JURISDICTION AND OPINIONS BELOW

The Opinion of the Supreme Court of the State of New Mexico, entered July 9, 1987, is reprinted as Appendix A at 1a-14a. The Order of the Supreme Court of the State of New Mexico, denying Southern Union Company's petition for rehearing, entered August 14, 1987, is reprinted as Appendix B at 15a. By order of Justice Byron R. White entered October 16, 1987, reprinted as Appendix H at 69a, the time for filing this petition was extended to December 12, 1987. The jurisdiction of this Court is invoked under 28 U.S.C. § 1257(3) (1982).

STATUTES INVOLVED

Relevant sections of the federal statutes involved herein, the Natural Gas Act of 1938, 15 U.S.C. §§ 717-17z (1982) ("NGA"), and the Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301-432 (1982) ("NGPA"), are reprinted as Appendices I and J, respectively, at 70a-80a and 81a-88a.

STATEMENT OF THE CASE

In 1979, respondent Consolidated Oil & Gas, Inc. ("Consolidated"), a producer of natural gas in New Mexico and sixteen other states, sued petitioner Southern Union Company ("Southern Union"), an integrated natural gas company, in New Mexico state court for breach of contract. The alleged breach was Southern Union's refusal to pay intrastate prices for gas sold under four interstate contracts as purportedly required by a 1976 agreement between the parties settling earlier contract litigation.

The case arose after twenty years of federally regulated and certificated sales of natural gas between the two companies.[1] In settlement of litigation over the operation of most favored nations clauses in intrastate contracts, involving in part both petitioner and respondent, Southern Union agreed to amend the pricing provisions of six contracts for sales of jurisdictionally intrastate gas. Consolidated requested, and Southern Union agreed, to add to the settlement agreement the four contracts for the sale of jurisdictionally interstate gas and to

[1] The facts and circumstances that unequivocally establish that the gas at issue in the litigation below was dedicated to interstate commerce and subject to federal price and abandonment controls are set forth in *Consolidated Oil & Gas, Inc.* v. *FERC*, 806 F.2d 275 (D.C. Cir. 1986), and the FERC orders it reviews (*Southern Union Gathering Co.*, 28 FERC ¶ 61,225 (Aug. 20, 1984), *Southern Union Gathering Co.*, 30 FERC ¶ 61,350 (Mar. 22, 1985), reprinted as Appendices C and D, respectively, at 16a-27a and 28a-41a).

amend their pricing provisions. The attorneys drafting and reviewing the agreement did not correct a discrepancy in the introductory statement that described all of the contracts covered by the settlement agreement as intrastate in nature. When Southern Union refused to pay the intrastate price on the four jurisdictionally interstate contracts that were subject to a lower federal ceiling rate, Consolidated sued for breach of the agreement, requesting the difference between the two rates in damages.

Beginning with its answer to the complaint, Southern Union maintained the defense that the damages sought by Consolidated are preempted by pervasive federal regulation of the rates for interstate natural gas sales, and that Federal Energy Regulatory Commission ("FERC") approval was a prerequisite to collection of the prices Consolidated seeks. In response to the complaint, therefore, Southern Union successfully urged the New Mexico trial court to seek the opinion of the FERC on the jurisdictional and preemption issues. In 1984, FERC ruled that the gas in question was jurisdictionally interstate (*see* note 1, *supra*), but refused to rule on Southern Union's preemption claim until after the New Mexico trial concluded. Citing *Arkansas Louisiana Gas Co.* v. *Hall*, 453 U.S. 571 (1981) ("*Arkla*"), the FERC stated, however, that "Consolidated would have no right under either the filed rate doctrine or its certificate authorization to collect a rate in excess of its contract rate or the applicable ceiling price, whichever is lower, in the absence of specific authority from this Commission." App. 25a.

After *Arkla*, Consolidated amended its New Mexico complaint to add a tort cause of action alleging that Southern Union negligently misrepresented that the gas contracts covered by the settlement agreement were not subject to federal regulation. Consolidated further claimed that it justifiably relied on the statement in entering into the settlement agreement and was damaged

in an amount equal to the difference between the interstate ceiling prices it was receiving for its gas and the intrastate prices it could have received if the four contracts were not subject to federal jurisdiction.[2]

In 1985, a New Mexico trial court found Southern Union liable under the negligent misrepresentation theory and awarded the damages originally sought by Consolidated under the contract claim. Judgment was for $11,023,967 plus post-judgment interest. *Consolidated Oil & Gas, Inc.* v. *Southern Union Co.*, Final Judgment, No. SF 79-2161(c) (July 12, 1985).[3] Southern Union appealed the trial court judgment directly to the New Mexico Supreme Court, which the applicable New Mexico rules require for contract cases. N.M. Stat. Ann. §§ 34-5-8, 34-5-14 (1984 Cum. Supp.), *In re Original Appellate Jurisdiction in the New Mexico Supreme Court & New Mexico Court of Appeals*, Misc. 8000 (Order of the New Mexico Supreme Court, April 20, 1983).

The New Mexico Supreme Court upheld the trial court judgment. With respect to the state negligence claim, the New Mexico court first acknowledged that, given the undeniable dedication of the disputed gas to interstate commerce and federal price regulation, "[t]here is thus no cause of action sounding in contract available to Consolidated to recover the intrastate prices promised in the Settlement Agreement." App. 8a-9a. But the New Mexico court concluded that under the New Mexico standard of negligence, Southern Union had a "fiduciary obligation" to provide Consolidated with accurate information about

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[2] According to a damage study prepared by Consolidated, the price differential, measured from 1976 through 1985 was $8,427,978, and that was the principal amount Consolidated sought and received as damages. Plaintiff's Exhibit 32.

[3] While Consolidated did not expressly amend the Complaint to drop the breach of contract claim, it did not brief or argue breach of contract issues at trial. The trial court also found an insufficient basis to award damages for fraud.

the jurisdictional status of its gas, and that Consolidated "reasonably" relied on Southern Union's inaccurate description of the gas in the settlement agreement. *Id.* at 11a.

The New Mexico court rejected Southern Union's federal preemption defense. It declared itself in agreement with an Order of the Federal Energy Regulatory Commission ("Commission") issued in an administrative proceeding,[4] that the preemption holding in *Arkla* was not applicable to the New Mexico trial court damage award for two reasons: *Arkla* was decided on the basis of the filed rate doctrine "which is inapplicable" to this case, and "tort damages do not conflict with federally regulated pricing." *Id.* at 12a. On August 14, 1987, the court denied Southern Union's Motion for Rehearing and granted a stay of execution of the judgment pending the outcome of this petition. App. 15a.

REASONS FOR GRANTING THE WRIT

Six years ago, in *Arkansas Louisiana Gas Co.* v. *Hall*, the Court found that the filed rate doctrine precluded a state court award of damages for breach of a sales

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[4] Following the trial court's decision in 1985, Southern Union petitioned the Commission for a declaratory order that because the damage award is, in effect, a rate increase, Consolidated cannot lawfully collect the damages absent Commission review and approval. On June 19, 1986, the Commission issued an order declaring that state court tort damage awards cannot violate the maximum lawful price provisions of the NGPA, nor interfere with the federal regulatory scheme. *Southern Union Co.*, 35 FERC ¶ 61,359 (1986), reprinted as Appendix E at 42a-55a. Southern Union's request for rehearing was denied, *Southern Union Co.*, 39 FERC ¶ 61,212 (May 22, 1987), reprinted as Appendix F at 56a-58a. After Southern Union sought review of that order from the U.S. Court of Appeals for the D.C. Circuit, the Commission reconsidered its ruling on its own motion, abandoned the principal rationale of its earlier ruling, but maintained its conclusion. *Southern Union Co.*, Nov. 20, 1987, reprinted as Appendix G at 59a-68a. Review continues in the D.C. Circuit where Southern Union has filed a motion for expedited consideration.

agreement that was tantamount to a rate increase for interstate natural gas sales. In that case, the defendant had neglected to inform the plaintiff of facts that made the rate increase appropriate under the contract, despite a duty to do so, and thus the plaintiff did not file an application with the FERC for a rate increase to which it was entitled. The Louisiana courts found that the defendant's conduct amounted to breach of contract, and awarded damages based on the difference between the federally-approved filed rate and the rate increase that the plaintiff would otherwise have filed. The Court struck down the award on the grounds that it interfered with exclusive federal regulatory authority over prices for interstate natural gas.

Southern Union respectfully submits that the Supreme Court of New Mexico has decided the federal question it faced in this case in direct conflict with the rule of *Arkla*. Both the logic and the holding of *Arkla* dictate that where state damage awards interfere with a federal scheme of rate regulation, the state action must yield to the federal scheme. The two distinctions advanced by the New Mexico court—that *Arkla* was a filed rate case, and was applicable only to contract cases—constitute a superficial and mistaken construction of *Arkla*. *Arkla* did not turn merely on whether the federal regulation is implemented by filed rates or some other mechanism established by Congress—in this case, the Natural Gas Policy Act. Nor did it turn on whether a state court labels a claim as tort or contract. Indeed, these distinctions conflict with preemption decisions of this Court that require a substantive inquiry into whether the state action interferes with the uniform scheme of gas regulation, and that preclude a state court's reliance on labels. *Arkla* is grounded, in fact, in basic preemption doctrine: that there can be no state interference with the mechanisms Congress has chosen to determine natural gas rates.

The New Mexico holding has ramifications well beyond the circumstances of this case. The state negligence standard, as applied to a regulated gas producer, is inconsistent with the duties imposed on producers by Congress under the NGA and the NGPA. Producers are required to have actual or constructive knowledge of the statutes and regulations that govern their interstate sales. The New Mexico holding is premised, however, on a producer's legal or "justifiable" reliance on a single misstatement concerning the status of its gas, one inconsistent with well over ten years of that producer's certificated gas sales in interstate commerce. App. 10a-11a.

Uniform regulation of natural gas companies will be impossible if states are free to evaluate their conduct in light of tort standards which are inconsistent with federal regulation of that conduct. Those companies would be subjected to different and possibly conflicting standards among the states, which would further undermine Congress' goal of uniformity. The Supremacy Clause mandates the preemption of inconsistent state standards of conduct such as the one imposed in New Mexico.

The *Arkla* Court recognized that a single exception to its holding might be appropriate, where "affirmative misconduct" formed the basis for the state court action, but the Court explicitly "save[d] for another day" resolution of that question. 453 U.S. at 583 & n.13. The possible exception for affirmative misconduct, however, contemplated more than simply a tort involving alleged negligence. Moreover, even if the New Mexico court correctly characterized this case as the one that *Arkla* "save[d] for another day," it misapplied the Court's precedent in the preemption area in analyzing the question *Arkla* reserved.

Certiorari or summary reversal is appropriate here because the New Mexico court failed to follow *Arkla* and did not undertake any analysis of the serious preemption

issues before it. Alternatively, the Court should grant certiorari here to resolve the question put aside six years ago.

A. The New Mexico Decision Misapplies *Arkansas Louisiana Gas Co.* v. *Hall* and Conflicts With Other Applicable Preemption Precedent

The paramount federal interest in the transportation and sales of natural gas has been affirmed by a long line of decisions of the Court, including *Arkla*. Beginning in 1954, the Court has upheld federal authority over independent producers of natural gas sold in interstate commerce, *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672 (1954), the primacy of federal authority over private contracts, *California* v. *Lo-Vaca Gathering Co.*, 379 U.S. 366 (1965), and even the dominance of the congressional decision to deregulate interstate gas prices over indirectly interfering state regulation. *Transcontinental Gas Pipe Line Corp.* v. *State Oil & Gas Bd.*, 474 U.S. 409 (1986). *Arkla* reaffirmed and clarified that federal occupation of the field of natural gas sales and rates precludes inconsistent state court contract claims. These and other cases have recognized the steadfast purpose of Congress to establish uniformity in the regulation of interstate natural gas sales.

While the goal of uniform regulation has remained constant, the method of regulation has changed over the years. Under the NGA, the Commission set price ceilings for sales from gas producers to pipelines and regulated the pipeline's rates to their downstream customers to insure that both sales prices and transportation rates were "just and reasonable." Through strict enforcement of gas sale certification and abandonment requirements, the Commission also acted to protect the supply of natural gas to interstate customers. In the late 1970's, Congress concluded that a new approach to natural gas regulation was needed, and adopted in the NGPA a "commodity value pricing approach." *Transcontinental*, 474 U.S. at

421. The federal role changed from sales certification and rate-making to overseeing a national, market-based regulatory scheme. Under the NGPA, producers may charge up to statutory ceiling prices and the prices are automatically passed through to consumers, unless the Commission decides otherwise. Although the method of regulation has changed, "The NGPA therefore does not constitute a federal retreat from a comprehensive gas policy" and interstate gas prices remain a "subject of deep federal concern." *Id.* at 421-22.

The New Mexico court acknowledged, as it must, the dominant federal interest in natural gas rates and correctly observed that had the award of damages to Consolidated been based on a breach of contract theory, it would have been preempted by direct application of *Arkla*. App. 12a. It nonetheless refused to apply *Arkla* because it construed that case as limited to breach of contract actions and to cases involving filed rates. Moreover, the court perceived no conflict between the trial court judgment and federal regulation.

1. Contrary to the New Mexico view, the Court's analysis in *Arkla* controls the analysis here. *Arkla* clearly focuses upon the relationship between state court damages and the congressional purpose behind comprehensive natural gas price regulation:

> It would undermine the congressional scheme of uniform rate regulation to allow a state court to award as damages a rate never filed with the Commission and thus never found to be reasonable within the meaning of the Act.

453 U.S. at 579. The *Arkla* framework thus requires consideration of whether a state court damage award reflects an attempt by parties "to vary by private agreement" federally regulated rates and thus to "undercut the clear purpose of the congressional scheme: granting the Commission an opportunity in every case to judge the reasonableness of the rate." *Id.* at 582.

The New Mexico court failed, in its one-page discussion of the preemption issue, to engage in the analysis that *Arkla* requires. See App. 12a. The court ignored clear signs that the suit was initiated to avoid federal price ceilings. In its 1979 complaint—filed two years before *Arkla*—Consolidated alleged that Southern Union had breached the settlement agreement by refusing to make payments in excess of the price ceilings imposed under the NGA and NGPA. Southern Union raised the jurisdictional defense in its answer, and filed a motion for a stay pending a decision by FERC, the proper forum for addressing the issues raised by Consolidated. Nearly five years later, after the Court issued its *Arkla* decision, Consolidated added its negligent misrepresentation claim and, on the eve of trial, all but abandoned its contract claim. *See* note 3, *supra.*

Consolidated proceeded to trial on its negligent misrepresentation theory. The trial court found Southern Union liable and awarded damages based on the difference between the interstate ceilings and the higher intrastate price referenced in the settlement agreement. This measure of damages, the difference between the contract rate and the federal ceiling rate, was the precise measure found unlawful in *Arkla.*[5]

Consolidated was an experienced producer of natural gas, and had engaged in interstate sales for decades.

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[5] The trial court adopted Consolidated's proposed measure of damages. Consolidated subtracted the interstate price applicable to gas sold from each well from the higher intrastate price provided for in the settlement agreement in order to arrive at a "price differential" for each well, *i.e.*, an amount in excess of the area ceiling rates, ranging from $.33 to $1.86 per Mcf. Consolidated multiplied the total volume produced from each well by the applicable price differential to arrive at an underpayment amount, and then added the underpayments for each well to arrive at a "total underpayment." *See* note 2, *supra.*

Consolidated signed applications for certificates of public convenience and necessity to the Commission—as required by federal law—to dedicate the gas in question to interstate jurisdiction. As an experienced producer, Consolidated knew, or is charged with knowing, that interstate gas can only be sold at the interstate price.

If these circumstances were not sufficient to alert the New Mexico court that it need undertake something more than a cursory approach to the preemption issue, Consolidated's own testimony should have provoked the court's scrutiny. Upon cross-examination, Consolidated's president conceded:

> Q. And your understanding of what that bargain was, Mr. Trueblood, . . . that they should pay you the intrastate price for interstate gas; that's [the] bargain?
>
> A. That's . . . in accordance with the bargain.
>
> Q. And that's the basic objective of this litigation; is that correct?
>
> A. Yes. That's the basic objective.

(R. 250-51).

Arkla, and additional preemption holdings of the Court, compel an analysis of these and other factors to determine whether the award of damages interferes with the comprehensive federal system of natural gas price regulation such that it must be preempted. The New Mexico court engaged in no analysis whatsoever, much less the one mandated by the Court. It did not consider the relationship between the tort claim, the damage award, and the applicable federal regulation. It ignored the significance of Consolidated's switch from contract to tort theory and the testimony of its president regarding the company's objectives.

With respect to the measure of damages, the New Mexico court merely concluded that "the trial court awarded damages, not as contract prices, but as consequences for tortious conduct." App. 12a. It thus shrugged off the fact that the measure of damages—the difference between the price Consolidated expected to receive under the settlement agreement and the federal ceiling prices paid by Southern Union—was a classic contract damage calculation, substantively indistinguishable from the invalid measure in *Arkla*. The New Mexico court characterized the damage award as recompense for settling the 1976 contract litigation, but in fact the award is not based on any evidence of harm suffered. It simply awards Consolidated the "benefit" of an unlawful "bargain." Under both the NGA and NGPA, had Southern Union paid, and Consolidated accepted, the prices referenced in the settlement agreement, they would have been in violation of those Acts and subject to their penalties. *See* App. 70a, 72a-73a, 80a, 83a-88a.

Finally, the New Mexico court relied on the *Gulftide* case, which involved punitive damages, because FERC had considered it controlling; FERC, however, discarded it as applicable precedent when it reconsidered its decision after the New Mexico court had ruled. *See* note 4, *supra*. Although FERC reached the same result as the New Mexico court, albeit through a different analysis, it relied on the premise that the New Mexico judiciary had adequately explored the facts. The problem is that neither forum has ever considered all of the facts in the context of the appropriate law, as this Court's decisions dictate. FERC and the New Mexico court have relied on one another's conclusions, and neither has undertaken an appropriate preemption analysis, which *Arkla* and other cases require and to which Southern Union is entitled. The Court should grant certiorari here to assure that the necessary analysis is performed.

2. The two grounds asserted by the New Mexico court for distinguishing *Arkla* find no support in the language of *Arkla* itself and conflict with other holdings of this Court. Indeed, the New Mexico court's reliance on one of those grounds—the filed rate doctrine—also raises a significant question as to whether the NGPA mechanism for regulating natural gas rates, which replaced FERC-approved filed rates and price ceilings with statutory price ceilings, extinguishes the precedential value of this Court's preemption decisions announced under the NGA.

The New Mexico court categorically distinguishes *Arkla* "because it was decided on the basis of the filed rate doctrine, which is inapplicable to the present proceeding." App. 12a. The court suggests that precedent regarding interference with the federal scheme of natural gas regulation in filed rate cases is inapplicable to this case and to any current or future cases involving allegations of interference with the statutory ceiling prices of the NGPA, notwithstanding the fact that the resulting interference with federal regulation may be equal or greater. The New Mexico court's overly restrictive reading of the filed rate doctrine would render those filed rate cases anachronisms, would frustrate congressional policy in the setting of natural gas prices, and would provide an impetus to a new wave of litigation testing the preemptive scope of the NGPA.

The filed rate doctrine initially was applied as a prohibition against courts adjudicating the reasonableness of rates in regulated industries and ordering deviations from filed rates; as the means used by Congress and the Commission to regulate rates has changed, however, the filed rate doctrine has grown to encompass other practices undermining agency rate-making authority. These practices include state agencies' ratable-take orders, *Transcontinental Gas Pipe Line Corp.* v. *State Oil & Gas Bd.*, 474 U.S. 409 (1986) and allocations of low-cost power between utilities. *Nantahala Power & Light Co.* v. *Thorn-*

burg, 106 S. Ct. 2349 (1986). These cases, decided after the enactment of the NGPA, indicate that the modern filed rate doctrine requires courts to analyze the purposes served by the federal regulatory scheme and determine whether the challenged state action interferes with those purposes. In refusing to perform that analysis in this case, the New Mexico court plainly and incorrectly implied that the preemption decisions under the NGA—the filed rate cases—do not apply to cases arising under the NGPA.

Fundamentally, the filed rate doctrine protects the operation of federally-established price regulating mechanisms, whatever form they take.[6] The doctrine traditionally has served to ensure that the statutory delegation of price setting authority to a regulatory agency is not undermined. There is no sense in the proposition asserted by the New Mexico court that the doctrine does not apply in principle to the NGPA price ceilings established by Congress itself.

The New Mexico court's dismissal of *Arkla* on filed rate grounds demonstrates its improper focus on labels rather than substance. Indeed, the New Mexico court disregarded this Court's recent express determination that the principle embodied in the filed rate doctrine has significance well beyond "filed" rates. In *Nantahala Power & Light Co.*, 106 S. Ct. at 2357, the Court held that "the filed rate doctrine is not limited to 'rates' *per se*," but rather applies in any situation where state action interferes with federal rate regulation:

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[6] The doctrine dates back as far as 1915, when the Court explicitly stated that even intentional misrepresentation would not justify the enforcement of contract rates deviating from federally approved rates. According to *Louisville & Nashville R.R.* v. *Maxwell*, 237 U.S. 94, 98 (1915), quoting *Kansas City S. Ry.* v. *Carl*, 227 U.S. 639, 653 (1913), "'[n]either the intentional nor accidental misstatement of the applicable published rate will bind'" the parties.

> The similarity between this case and the more typical application of the filed-rate doctrine is apparent from the impermissible interference that enforcement of NCUC's order would create with the scheme of federal regulation.

Id. at 2359. As the Court noted in *Transcontinental Gas Pipe Line Corp.*, the passage of the Natural Gas Policy Act in 1978 changed the mechanism for rate regulation but left untouched the principle of exclusive federal jurisdiction over wholesale gas rates.[7] The importance of confirming the applicability of the filed rate principle to preemption analysis under the NGPA merits the Court's review of this case.

3. The second basis articulated in the New Mexico decision for not applying *Arkla* also conflicts with the policies enunciated by this Court. According to the New Mexico court, because this case involves damages "for tortious conduct," the decision here is not contrary to a congressionally established scheme, as was the damage award for breach of contract in *Arkla*. *Arkla* cannot reasonably be read to hang on such a flimsy tort/contract hook. Even narrowly construed, *Arkla* stands for the proposition that a state court damage award—in contract or tort—which conflicts with federal requirements for the regulation of natural gas cannot stand. As the *Arkla* Court observed, "when Congress has established an exclusive form of regulation, 'there can be no divided authority over interstate commerce.'" *Arkla* at 580, quoting *Missouri Pacific R.R. v. Stroud*, 267 U.S. 404, 408

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[7] Under regulations implementing the NGA in 1971, the price of Consolidated's sales, as a regulated seller of natural gas, was limited not by filed rates, but by a small-producer certificate. A "small producer" certificate exempted a "small producer" (as defined by the Commission's regulations) from having to file a rate schedule as long as the increase in rate did not exceed the ceiling rate set by the Commission. *See* 18 C.F.R. § 157.40 (1987). After 1978, under the NGPA, Consolidated could charge no more than the statutory—as opposed to the certificate's—ceiling rates for its gas.

(1925). Thus, when a state decision sounding in tort imposes a standard of conduct "at odds with the uniformity contemplated by Congress," it is preempted. *Arkla* at 580, citing *Chicago & N.W. Transp. Co.* v. *Kalo Brick & Tile Co.*, 450 U.S. 311 (1981).

This Court has long emphasized, in preemption decisions, the *nature* of the state court action and the interests, rights, and obligations at stake, rather than the legal label:

> [O]ur cases "demonstrate that the decision to preempt federal and state court jurisdiction over a given class of cases must depend upon the nature of the particular interests being asserted and the effect upon the administration of national labor policies of concurrent judicial and administrative remedies."

Farmer v. *United Brotherhood of Carpenters*, 430 U.S. 290, 300-301 (1977), citing *Vaca* v. *Sipes*, 386 U.S. 171, 180 (1967). *See also Amalgamated Ass'n of Street, Electric Ry. & Motor Coach Employees* v. *Lockridge*, 403 U.S. 274, 292 (1971) ("It is the conduct being regulated, not the formal description of governing legal standards, that is the proper focus of concern."). As the Court observed in *International Brotherhood of Electrical Workers, AFL-CIO* v. *Hechler*, 107 S. Ct. 2161 (1987), a litigant cannot escape the Supremacy Clause by a clever casting of its claim. *See also Olguin* v. *Inspiration Consolidated Copper Co.*, 740 F.2d 1468 (9th Cir. 1984) (invoking the "artful pleading doctrine" in holding a state law claim preempted); *Young* v. *Anthony's Fish Grottos, Inc.*, 830 F.2d 993, 999 (9th Cir. 1987) ("The key to determining the scope of preemption is not how the complaint is cast, but whether the claims can be resolved only by referring to the terms of the collective bargaining agreement.").

Indeed, the key issue in *Arkla* was whether the state court action undermined uniformity established by a federal regulatory scheme, not the label attached to the

claim brought in the state court. In *Kalo Brick & Tile, Co.*, decided the same term and cited in *Arkla*, the Court held that a tort action for damages resulting from the cessation of service by a rail carrier was preempted. The Court determined that allowing a state to impose its own legal requirements on carriers regulated by the federal government "could hardly be more at odds with the uniformity contemplated by Congress in enacting the Interstate Commerce Act." 450 U.S. at 326.

The Court reiterated these principles in two recent labor law preemption cases. In *Allis-Chalmers Corp.* v. *Lueck*, 471 U.S. 202, 213 (1985), the Court held that a preemption analysis must focus on whether evaluation of the state tort claim is "inextricably intertwined with consideration of the terms of the . . . contract." Late last term, in *International Brotherhood of Electrical Workers*, 107 S. Ct. at 2168, the Court reaffirmed that the "need for federal uniformity . . . therefore mandates that here, as in *Allis-Chalmers*, respondent is precluded from evading the pre-emptive force of § 301 by casting her claim as a state-law tort action." [8]

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[8] The New Mexico decision would provide an incentive and opportunity for producers throughout the country to recast contractually based claims for relief in areas which continue to be preempted under the NGPA as tort claims in order to circumvent federal regulation. Commentators have noted the increasing convergence of tort and contract causes of action, which will facilitate the opportunities to avert a contract bar by couching a claim in tort. *See* Note, *Tort Remedies for Breach of Contract: The Expansion of Tortious Breach of the Implied Covenant of Good Faith and Fair Dealing into the Commercial Realm*, 86 Colum. L. Rev. 377, 401 (1986), G. Gilmore, *The Death of Contract* (1974). It bears noting, in this regard, that the *Arkla* plaintiffs could today frame their pleading as a tort such as breach of the covenant of good faith, a tort recognized in an increasing number of states. *See, e.g., Seaman's Direct Buying Service, Inc.* v. *Standard Oil Co.*, 36 Cal. 3d 752, 686 P.2d 1158, 206 Cal. Rptr. 354 (1984); *EKE Builders, Inc.* v. *Quail Bluff Assocs.*, 714 P.2d 604 (Okla. Ct. App. 1985). Under the New Mexico court's approach, the *Arkla* plain-

The proper inquiry, therefore, does not stop with the form of the claim but must examine whether, as the Court noted in *Allis-Chalmers*, the state court award is "inextricably intertwined" with the federal regulatory regime. The New Mexico court, however, simply drew an artificial tort/contract line. In so doing, the New Mexico court purported to rely on *Arkla* even though *Arkla* neither draws nor implies any such superficial distinction and actually cites a tort preemption case, *Kalo Brick & Tile Co.*, for support. Indeed, it would be remarkable for *Arkla* to stand for such a distinction in light of the Court's other precedent consistently rejecting a categorical analysis in favor of an analysis of the substantive nature of the claim. However desirable it may be to simplify preemption analysis, it cannot be simplified to the point of ignoring the effect of the state action on the federal regulatory system. The New Mexico decision conflicts with the teachings of this Court. The Court should review that decision to reaffirm that Supremacy Clause determinations depend not on form, but on substance.

B. The New Mexico Negligence Standard As Applied Here Is Inconsistent With Uniform Federal Regulation of Natural Gas Sales

Southern Union seeks certiorari in part, as discussed above, because the New Mexico decision conflicts with applicable precedent of this Court. In addition, however, this case warrants certiorari because it independently presents important issues bearing on uniform federal regulation of the gas industry. The New Mexico decision rests on a premise at odds with the concept that all regulated producers are required to know and understand regulatory requirements governing interstate natural gas sales. To find Southern Union liable for negligent mis-

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tiffs would be able to collect damages based on that claim, even if they were measured in the precise way the contract damages in *Arkla* were calculated.

representation under the state standard for negligence, the New Mexico court had to find that Consolidated justifiably relied on the mistaken introductory statement. This determination turns principally on an analysis of Consolidated's obligations and responsibilities as a producer and seller of interstate gas subject to federal regulation. The New Mexico decision on this point assumes, contrary to federal regulation, that a natural gas company may lawfully be ignorant of the jurisdictional status of its gas.

Uniform administration of the NGA and the NGPA depends on the presumption that producers know and conform to the Acts' requirements. An entire section of the Code of Federal Regulations details the obligations of producers to report jurisdictional sales and, depending on the form of rate regulation in effect during the sales period, to charge no more than approved or ceiling rates for the gas. *See* 18 C.F.R. Parts 274, 275 (1987). Under the NGA, once a producer began reporting jurisdictional sales, it could not simply decide that the sales were not, in fact, jurisdictional, and cease complying with federal regulations; it had to seek Commission approval for any change in rates or service.[9] Similarly, only the Commission can approve an increase in the NGPA ceiling rates.[10]

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[9] The NGA provides that a natural gas company subject to its jurisdiction may only charge "just and reasonable rates," 15 U.S.C. § 717c(a) (1982) (App. 72a), that rates must be filed with the Commission "in such form as the Commission may designate," *id.* at § 717c(c) (App. 73a), and that no one may make or abandon interstate sales for resale without Commission approval. 15 U.S.C. § 717f (1982). App. 76a-79a.

[10] The NGPA provides that "[i]t shall be unlawful for any person . . . to sell natural gas at a first sale price in excess of any applicable maximum lawful price under this chapter." 15 U.S.C. § 3414(a) (1982). The Commission has authority, however, to approve higher than maximum lawful prices for gas dedicated to interstate commerce prior to the NGPA if the higher price is "just and reasonable" within the meaning of the NGA. 15 U.S.C. § 3314(b)(2) (1982). App. 83a-84a. Most of the Consolidated gas

As with other areas of the law, natural gas producers are charged with constructive knowledge of statutes, regulations and orders that affect their operations.[11] The New Mexico court nonetheless found that Consolidated, as a federally regulated producer, was justified in relying on an erroneous introductory statement regarding the jurisdictional status of the gas.

The obligations of producers are so intrinsic to the uniform federal scheme that it would create havoc to allow each state to impose a different standard of conduct on producers of natural gas. There would not only be differences between federal and state obligations, but inconsistent standards of conduct among the states themselves.

There is no question here that Consolidated could have resolved its rate dispute with Southern Union in proceedings before the Commission. *See* note 10, *supra*. That route is the appropriate and exclusive one under the federal scheme. *See* App. 25a-26a. By transforming its claim for a higher rate into a state court negligence claim, Consolidated was able to avoid demonstrating that its collection of the higher rate would satisfy the statutory standard that the rate be "just and reasonable." Indeed, the New Mexico state court has no jurisdiction to make such a determination. *See Arkla* at 577. By per-

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at issue here was dedicated to interstate commerce prior to 1978. Some of the gas was produced from wells drilled after the NGPA, and the Commission does not have express statutory authority to permit price increases for that gas. 15 U.S.C. § 3313. *See* App. 81a-82a.

[11] Under the NGPA, any person who "knowingly" violates any provisions of the act may be subject to civil or criminal penalties. 15 U.S.C. § 3414(b), (c) (1982). "Knowing" is defined to mean having "the constructive knowledge deemed to be possesed by a reasonable individual who acts under similar circumstances." 15 U.S.C. § 3414(b)(6)(B)(ii), (c)(5)(B) (1982). App. 84a-88a.

suading the New Mexico courts to approve a lower standard of conduct for a producer, one that effectively discards constructive knowledge of federal regulatory requirements, Consolidated has avoided the appropriate administrative forum. In the process, the New Mexico court has decided incorrectly an issue with serious implications for uniform natural gas regulation.

C. Alternatively, This Case Presents the Issue Expressly Left Unresolved in *Arkansas Louisiana Gas Co.* v. *Hall*

This case may be appropriate for review on the alternative ground that it presents the issue that the *Arkla* Court expressly left unanswered six years ago:

> [W]e are not faced with affirmative misconduct, and we need not consider the application of the filed rate doctrine in such a case.

453 U.S. at 582. The *Arkla* opinion explicitly "save[d] for another day" the question of whether the filed rate doctrine "applies in the face of fraudulent conduct." *Id.*, n.13.

The opinion of the New Mexico Supreme Court treats this case as presenting the unresolved issue of *Arkansas Louisiana* v. *Hall* and thus falling outside the *Arkla* ruling:

> The Supreme Court stated that federal regulation would be undermined if state courts could authorize contractual agreements contrary to a congressionally established scheme. There was no finding in *Arkla*, however, of any intentional misconduct by defendants. In the present case, the trial court awarded damages, not as contract prices, but as consequences for tortious conduct. For this reason, too, *Arkla* does not provide precedent for the case at bar.

As discussed above, *Arkla* is controlling precedent here. The language of the *Arkla* Court regarding the possible exception to its scope dealt only with affirmative miscon-

duct such as fraud. This possible exception for "affirmative misconduct" or "fraudulent conduct" requires something more than negligence, as numerous courts have held in other settings.[12] The possible exception noted in *Arkla* appears more likely to be the one that the Court has elsewhere carved out in federal preemption cases for particularly egregious conduct. *See Farmer* v. *United Brotherhood of Carpenters*, 430 U.S. at 302 (excluding from preemption tortious misconduct which "no reasonable man in a civilized society should be expected to endure").

Nevertheless, if the New Mexico court is correct that this was the issue left unresolved by *Arkla*, this is a particularly appropriate case for the Court to review in order to address that question since it involves interference with federal regulation of natural gas. *Arkla* did involve breach of contract, not tort, and the Court has never expressly extended its reach to tort damage awards. While Southern Union submits that *Arkla*, by dint of its logic and by analogy from other Court precedent, *e.g.*, *Allis-Chalmers*, must apply in negligence cases, it respectfully requests that the Court grant certiorari on the alternative ground that *Arkla*'s applicability to tort cases was the issue "save[d] for another day."

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[12] *Jaa* v. *INS*, 779 F.2d 569, 572 (9th Cir. 1986); *TRW, Inc.* v. *FTC*, 647 F.2d 942, 951 (9th Cir. 1981) (defining affirmative misconduct as "something more than mere negligence"); *Portmann* v. *United States*, 674 F.2d 1155, 1167 (7th Cir. 1982); *Green* v. *United States Dept. of Labor*, 775 F.2d 964, 970 (8th Cir. 1985); *Sederquist* v. *Tahoe Regional Planning Agency*, 652 F. Supp. 341, 347 (D. Nev. 1987) ("affirmative misconduct must be more than negligence.").

CONCLUSION

For the foregoing reasons, petitioner respectfully prays that the Court issue a writ of certiorari to review the judgment of the Supreme Court of the State of New Mexico.

Respectfully submitted,

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